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Supreme Court, U. S.

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In the Supreme Court of the United States
OCTOBER TERM, 1977

UNITED STATES OF AMERICA, PETITIONER

v.

ONOFRE J. SOTELO and NAOMI SOTELO

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES

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BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the bankruptcy judge (Pet. App. A, pp. 1a-14a) and the decision and order of the district court (Pet. App. B, pp. 15a-16a) are not officially reported. The opinion of the court of appeals (Pet. App. C, pp. 17a-22a) is reported at 551 F.2d 1090.

JURISDICTION

The judgment of the court of appeals was entered on March 24, 1977 (Pet. App. D, pp. 23a-24a). The

petition for a writ of certiorari was filed on June 7, 1977, and was granted on October 3, 1977 (App. B, *infra*, p. 13a).¹ The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the liability equal to unpaid taxes withheld from employees' wages that is imposed by Section 6672 of the Internal Revenue Code of 1954 upon persons who are required to collect and pay over such taxes but who willfully fail to do so, is dischargeable under Section 17 of the Bankruptcy Act.

STATUTES INVOLVED

Sections 3101, 3102, 3402, 3403, 6671, 6672, and 7501 of the Internal Revenue Code of 1954 (26 U.S.C.) and Section 17 of the Bankruptcy Act (11 U.S.C. 35) are set forth in Appendix A, *infra*, pp. 1a-5a.

STATEMENT

On June 26, 1973, O. J. Sotelo and Son Masonry Inc., a corporation, was adjudicated a bankrupt. Respondents Onofre J. Sotelo and his wife, Naomi Sotelo, served respectively as president (chief executive offi-

¹ On October 31, 1977, the Court granted the government's motion to dispense with the requirement of a separate appendix. Accordingly, we have set forth in Appendix B, *infra*, pp. 6a-13a, the docket entries of the lower courts, the notices of appeal to the lower courts, and the order allowing certiorari.

cer) and secretary of the corporation (Pet. App. A, p. 1a). Shortly thereafter, on July 5, 1973, respondents were adjudicated bankrupts on their voluntary petitions and their individual bankruptcy proceedings were consolidated (Pet. App. A, p. 1a).

On November 5, 1973, the government filed a claim in the consolidated individual bankruptcy cases for \$40,751.16² for unpaid taxes withheld from the corporation's employees, penalties, and interest. The government's tax claim was based upon respondents' liability as corporate officers under Section 6672 of the Internal Revenue Code of 1954, which imposes personal liability for unpaid withholding taxes upon persons responsible for collecting and paying over taxes withheld from employees' wages, but who willfully fail to do so (Pet. App. A, pp. 1a-2a).

Respondents objected to the claim on the ground that neither was an officer of the corporation who was responsible for collecting and paying over to the government the withholding taxes. The trustee objected to the government's claim on the ground that the withholding tax liability was a corporate obligation that was not personally guaranteed by the bankrupts (Pet. App. A, p. 2a).

Following a trial of these issues, the bankruptcy judge found that respondent Onofre J. Sotelo, in his

² The bankruptcy court allowed the government's claim to the extent of \$32,840.71 (Pet. App. A, p. 2a).

capacity as chief executive officer and majority stockholder of the corporation, had been responsible to collect and pay over the withholding taxes and was therefore personally liable for the taxes under Section 6672 of the Code. However, the bankruptcy judge further found that respondent Naomi Sotelo was not personally liable for the taxes because she had not been responsible for their collection and payment (Pet. App. A, p. 2a).

The assets of the bankruptcy estate were insufficient to satisfy the government's tax claim. Accordingly, the government served a notice of levy on the trustee with respect to \$10,000 that had been set aside as respondent Onofre J. Sotelo's homestead exemption under state law (Pet. App. A, pp. 3a-4a).^{*} The trustee thereafter sought an order from the bankruptcy judge directing that the homestead funds be paid to the government (Pet. App. A, p. 4a). However, respondents objected to the payment of the \$10,000 to the government on the ground that the homestead exemption belonged to respondent Naomi Sotelo. Respondents also urged that the liability for unpaid withholding taxes under Section 6672 was a dischargeable compensatory penalty rather than a tax (Pet. App. A, pp. 4a, 10a).

^{*} Prior to the date on which the government filed its claim, the trustee allowed respondent Onofre J. Sotelo a homestead exemption in certain real estate which respondents held as joint tenants (Pet. App. A, p. 3a). The real estate was sold subject to certain liens, and the trustee set aside \$10,000 as Onofre J. Sotelo's homestead exemption (Pet. App. A, p. 3a). See Smith-Hurd Ill. Ann. Stat., c. 52, Section 1 (1977 Cum. Supp.).

The bankruptcy judge held that respondent Onofre J. Sotelo's Section 6672 liability was a non-dischargeable tax under Section 17a of the Bankruptcy Act, and that the homestead exemption belonged solely to him, as the head of the household (Pet. App. A, pp. 6a-9a, 10a-12a). The district court affirmed on the basis of the opinion of the bankruptcy judge (Pet. App. B, pp. 15a-16a).

The court of appeals reversed. It held that the liability imposed by Section 6672 was a debt that was dischargeable in respondent's personal bankruptcy and was not a non-dischargeable tax (Pet. App. C, pp. 19a, 22a). In the court of appeals' view, the use of the word "penalty" in Section 6672 to describe the liability of a responsible officer to pay unpaid withholding taxes showed that the government's claim was not for a tax. In so holding, the court acknowledged that its decision conflicted with *Murphy v. Internal Revenue Service*, 533 F.2d 941 (C.A. 5), affirming 381 F. Supp. 813 (N.D. Ala.), and those of many lower courts that Section 6672 was a collection device and the liability it imposed equal to unpaid withholding taxes was a non-dischargeable "tax" within the meaning of Section 17a(1) of the Bankruptcy Act (Pet. App. C, p. 19a; see also *id.* at p. 22a n. 4).

The court rejected the government's further argument that the liability was non-dischargeable under Section 17a(1)(e) of the Bankruptcy Act, which provides that taxes "which the bankrupt has collected or withheld from others as required by the laws of the United States * * * but has not paid over" shall not

be dischargeable. The court concluded that Section 17a(1)(e) was inapplicable because respondent's Section 6672 liability was for a "penalty" and not a "tax" and because the corporation and not respondent was required to collect and pay over the withholding taxes in the first instance (Pet. App. C, pp. 20a-21a).⁴

SUMMARY OF ARGUMENT

Section 6672 of the Internal Revenue Code of 1954 provides that "Any person required to collect * * * and pay over any tax * * * who willfully fails to collect such tax, or truthfully account for and pay over such tax, * * * shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over." The purpose of the statute is to impose personal liability upon those whose control of the financial affairs of a business entity requires them to collect and pay over taxes collected from third parties.

The decision of the court of appeals that the liability imposed by Section 6672 for unpaid withholding taxes is dischargeable in the bankruptcy of the person

⁴ The court of appeals believed that by holding that the government's tax liability was dischargeable, it did not have to consider respondent Onofre Sotelo's alternative contention that his wife Naomi Sotelo was entitled to a state homestead exemption free from her husband's Section 6672 liability (Pet. App. C, p. 22a, n. 3). However, that conclusion was erroneous. As we shall explain *infra*, pp. 33-34, n. 23, the case must in all events be remanded to the court of appeals to address respondents' homestead argument.

who willfully failed to pay over such taxes is erroneous on two independent grounds.

A.

Section 17a(1)(e) of the Bankruptcy Act bars a discharge of a bankrupt's Section 6672 liability for unpaid withholding taxes. That statute directs that "discharge in bankruptcy shall not release a bankrupt from any taxes * * * which the bankrupt has collected or withheld from others as required by the laws of the United States * * * but has not paid over * * *." The language of Section 17a(1)(e) is explicit and controls this case. Since respondent had withheld but not paid over taxes from the wages of his corporation's employees, pursuant to the requirements of 29 U.S.C. 3402, Section 3402 of the Internal Revenue Code, the liability imposed by Section 6672 upon him to pay such taxes is not dischargeable in bankruptcy.

The legislative history of Section 17a(1)(e) confirms that Congress intended that a corporate officer's Section 6672 liability is not dischargeable in bankruptcy. Prior to the 1966 amendment adding subsection (e) to Section 17, the Treasury had consistently objected to proposals before Congress that would have made the Section 6672 liability dischargeable in bankruptcy. Although Congress initially declined to adopt the Treasury's position in the belief that the enactment of a criminal penalty would suffice, in 1966 it provided explicitly for the non-dischargeability of such trust fund taxes.

In light of this legislative history, there is no basis for the court of appeals' conclusion that Section 17a(1)(e) applies only to the corporate employer and not to the Section 6672 liability of the officer responsible for the collection and payment of withheld taxes. Indeed, there would have been little reason for Congress to render non-dischargeable the corporate employer's obligation to pay withholding taxes, since it was fully aware that for all practical purposes a corporation ceases to exist after a liquidating bankruptcy. In providing for the non-dischargeability of "taxes * * * which the bankrupt has collected or withheld from others," Congress intended that the obligation to pay over such taxes that Section 6672 imposes upon a corporate officer such as respondent survive his personal bankruptcy.

B.

The court of appeals also erred in holding that respondent's Section 6672 liability was a dischargeable compensatory "penalty" rather than a non-dischargeable obligation for "taxes * * * legally due and owing by the bankrupt to the United States * * *" within the meaning of Section 17a(1) of the Bankruptcy Act. In so concluding, the court relied upon the use of the word "penalty" in Section 6672 to describe a corporate officer's personal obligation for unpaid taxes withheld from the wages of the corporation's employees.

But until the decision below, the courts of appeals had uniformly recognized that the purpose of Section 6672 is not to penalize in the usual sense of that term but simply to collect what are undisputably taxes. The liability Section 6672 imposes is therefore a "tax" despite its nomenclature as a "penalty." An unbroken line of decisions of this Court that the term "tax" as used in the Bankruptcy Act refers to "a pecuniary burden laid upon individuals or property for the purpose of supporting the Government * * *" supports our submission that the Section 6672 liability is a non-dischargeable "tax" under Section 17a(1). *New Jersey v. Anderson*, 203 U.S. 483, 492. Accord: *United States v. New York*, 315 U.S. 510, 515-516; *New York v. Feiring*, 313 U.S. 283, 287.

ARGUMENT

THE LIABILITY IMPOSED BY SECTION 6672 OF THE INTERNAL REVENUE CODE UPON PERSONS WHO ARE REQUIRED TO COLLECT AND PAY OVER TAXES WITHHELD FROM EMPLOYEES' WAGES BUT WHO WILLFULLY FAIL TO DO SO IS NOT DISCHARGEABLE UNDER SECTION 17 OF THE BANKRUPTCY ACT

A. Introduction

1. This federal tax case presents a question of considerable importance to the administration of the withholding tax system and the Bankruptcy Act. Since 1942, the collection of income taxes by withholding at the source has been an integral part of the internal revenue laws. As a practical matter, Con-

gress recognized that many persons found it difficult to pay their tax liabilities at the time they filed their returns after the close of the taxable year. By requiring withholding of taxes at the source, Congress sought to prevent the loss of large amounts of revenue that would not be collected between the receipt of income and the filing of the returns reporting such income.⁸ The importance of this method of collecting is shown by the fact that withholding taxes on wages recently accounted for 83 percent of the total amount of individual income tax collections.⁹

The current statutory provisions are set forth in Sections 3402-3403 of the Internal Revenue Code of 1954, as amended, Appendix A, *infra*, pp. 2a-3a. Section 3402(a) provides that "[e]very employer making payment of wages shall deduct and withhold upon such wages" a tax determined in accordance with tables prescribed by the Secretary. Pursuant to Section 3403, "[t]he employer shall be liable for the payment of the tax required to be deducted and with-

⁸ See Revenue Act of 1942, Section 172, 56 Stat. 884; Current Tax Payment Act of 1943, 57 Stat. 126; H.R. Doc. No. 237, 78th Cong., 1st Sess. 1 (1943); H.R. Rep. No. 268, 78th Cong., 1st Sess. 1-2 (1943). See also *United States v. American Friends Service Committee*, 419 U.S. 7, 10.

⁹ *Annual Report of the Commissioner of Internal Revenue*, p. 137 (1976).

¹⁰ There are similar provisions governing the collection of social security taxes. Section 3102(a) places the duty of collection upon the employer; Section 3102(b) imposes personal liability for the tax upon the employer. See Appendix A, *infra*, p. 2a. See also Section 3202 (Railroad Retirement

held * * *." Section 7501 provides that the withheld taxes "shall be held to be a special fund in trust for the United States." Appendix A, *infra*, p. 4a.^{*}

In imposing the collection obligation and the liability for withheld taxes upon the employer, Congress recognized that corporate employers could fail to set aside and pay over these taxes to the government. If the corporation proved unable to pay the taxes, the Treasury would suffer the loss because the employees from whose wages the taxes are withheld would still be credited with those amounts against their tax liability as if they were in fact paid over to the government. *Dillard v. Patterson*, 326 F.2d 302, 304 (C.A. 5); *Moore v. United States*, 465 F.2d 514, 517-518 (C.A. 5), certiorari denied, 409 U.S. 1108; *Hariman v. United States*, 538 F.2d 1336, 1340 (C.A. 8).

Accordingly, Congress sought to insure against such a result by imposing personal liability for withholding taxes upon those whose control of the financial affairs of a business entity requires them to collect and pay over taxes collected from third parties. Section 6672 of the Code, Appendix A, *infra*, pp. 3a-4a, provides that "Any person required to collect * * * and pay over any tax * * * who willfully fails to

Act taxes). Furthermore, the Code requires sellers and others to collect and pay over certain excise taxes. See, e.g., 26 U.S.C. 4061, *et seq.*

^{*} See also *Newsome v. United States*, 431 F.2d 742, 745-746 (C.A. 5), certiorari denied, 411 U.S. 986; *Kalb v. United States*, 505 F.2d 506, 509 (C.A. 2), certiorari denied, 421 U.S. 979; *Harrington v. United States*, 504 F.2d 1306, 1311 (C.A. 1); *High v. United States*, 506 F.2d 755, 756 (C.A. 5).

collect such tax, or truthfully account for and pay over such tax, * * * shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over." Section 6671(b) defines the statutory term "person" to include "an officer or employee of a corporation, or a member or employee of a partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs." *

2. It is undisputed that under the foregoing statutory provisions, O. J. Sotelo and Son Masonry, Inc., as an employer, was required to collect and with-

* Section 6671(b) specifies that the term "person" required to collect or withhold taxes "includes an officer or employee of a corporation, or a member or employee of a partnership." The section is not limited, therefore, to officers and employees of a corporation. See, *Groman v. Commissioner*, 302 U.S. 82, 86, in which this Court stated in connection with analogous terminology, "when an exclusive definition is intended the word 'means' is employed, * * * whereas here the word used is 'includes'. If more were needed § 701(b) declares: 'The terms 'includes' and 'including' when used in a definition contained in this Act shall not be deemed to exclude other things otherwise within the meaning of the term defined.'" See also 26 U.S.C. 7701(b), the equivalent provision in the 1954 Code.

Thus, while Section 6672 is most frequently invoked against corporate officers, the provision has been held to apply to partners, lenders, and others. See, e.g., *Mueller v. Nixon*, 470 F.2d 1348, 1349-1350 (C.A. 6), certiorari denied, 412 U.S. 949 (officer of a second corporation); *Adams v. United States*, 504 F.2d 73, 75-76 (C.A. 7) (finance company); *Pacific National Ins. Co. v. United States*, 422 F.2d 26, 29-30 (C.A. 9), certiorari denied, 398 U.S. 937 (surety); *Werner v. United States*, 512 F.2d 1381, 1382 (C.A. 2), affirming 374 F. Supp. 558 (D. Conn.) (creditor); *Genins v. United States*, 489 F.2d 95, 96 (C.A. 5) (partner).

hold income and social security taxes from its employees and was liable for the payment of the taxes withheld. Moreover, respondent Onofre Sotelo does not deny that he was a person responsible for the collection and payment of such taxes from the employees of his corporation and that his failure to do so triggered his personal liability under Section 6672 (see Pet. App. C, p. 18a). However, respondent contends, and the court of appeals held, that his liability for the unpaid withholding taxes is dischargeable in his subsequent personal bankruptcy."

As we shall show, the decision of the court of appeals rests upon two erroneous grounds and reversal on either of these grounds is an independent basis for reversal of its judgment.

1. In holding that respondent's Section 6672 liability was dischargeable in his personal bankruptcy, the court of appeals refused to apply Section 17a (1)(e) of the Bankruptcy Act, which bars a discharge for withholding tax obligations of the type at issue here.

¹⁰ *Slodov v. United States*, certiorari granted, October 3, 1977 (No. 76-1835), which is set for oral argument in tandem with this case, also arose in the context of a personal bankruptcy proceeding. There, the question is whether an officer of a corporation was a person responsible for payment of withholding taxes who willfully failed to do so, and therefore liable for the unpaid taxes under Section 6672. In *Slodov*, the bankrupt does not assert that the government's claim for unpaid withholding taxes is dischargeable in bankruptcy. We are serving a copy of this brief upon counsel for the petitioner in *Slodov*.

2. Alternatively, the court of appeals erred in holding that respondent's Section 6672 liability was a dischargeable "penalty" rather than a non-dischargeable obligation for "taxes * * * legally due and owing by the bankrupt to the United States" within the meaning of Section 17a(1) of the Bankruptcy Act. Since Section 6672 is a device to collect what are indisputably taxes, the liability it imposes upon persons responsible for their collection and payment is likewise a non-dischargeable "tax" within the meaning of Section 17a(1).

B. Section 17a(1)(e) Of The Bankruptcy Act Bars A Discharge Of A Bankrupt's Liability For Taxes That He Is Required To Withhold From Third Parties

1. Section 17a(1)(e) of the Bankruptcy Act, Appendix A, *infra*, pp. 4a-5a, states that "a discharge in bankruptcy shall not release a bankrupt from any taxes * * * which the bankrupt has collected or withheld from others as required by the laws of the United States * * *." The language of this provision is explicit and controls this case. It bars a discharge of the liability imposed upon an officer of a corporation who is required to withhold and pay over taxes from the wages of the corporation's employees.

Respondents' corporation had withheld taxes from the wages of its employees, pursuant to the requirements of 26 U.S.C. 3402. As a responsible officer of his corporation, respondent Onofre Sotelo was required, by 26 U.S.C. 6671(b) and 6672, to collect and pay over the withholding taxes of his corporation

and is personally liable for his failure to do so. Under these circumstances, Section 17a(1)(e) directs that the liability imposed by Section 6672 upon such an officer of a business entity to pay such taxes is not dischargeable in bankruptcy.

The legislative history of Section 17a(1)(e) confirms that Congress intended that a corporate officer's Section 6672 liability for withholding taxes would not be dischargeable in bankruptcy. Prior to the 1966 amendment of Section 17, the Treasury Department had consistently objected to proposals in Congress that would have made the Section 6672 liability dischargeable in bankruptcy. As the Treasury pointed out to the House Committee on the Judiciary with respect to a proposed revision of Section 17 (H.R. Rep. No. 2535, 85th Cong., 2d Sess. 6 (1958)):

The kind of overhanging liability frequently encountered in bankruptcy cases is not primarily income tax but often includes substantial amounts of withholding taxes deducted from employees' wages and salaries, as well as social security and unemployment taxes, and excise taxes. Some of these unpaid tax liabilities, therefore, represent amounts withheld [*sic*] from employees or other persons which are legally held in trust for the Government. The proposal would thus discharge or reduce the priority of liabilities resulting not from the bankrupt's failure to pay his own taxes but from his failure to keep intact money which he had obtained from others as a trustee for the Government.

Congress initially declined to adopt the Treasury's position in favor of non-dischargeability of trust fund taxes in the belief that a criminal penalty (26 U.S.C. 7215) against responsible persons who fail to pay over such taxes would be an effective deterrent to avoidance of withholding tax obligations. As the House Committee observed (H.R. Rep. No. 2535, *supra*, at 5)—

Proposals to limit the priority and nondischargeability of taxes have been criticized on the ground that they would release a bankrupt from liability for tax money which he had withheld from others but had not paid over to the Government. The argument has been substantially weakened by the enactment during this Congress of Public Law 85-321. That act provides criminal penalties against anyone who, after notice by the United States, fails to deposit withholding taxes in an account in trust for the United States.

See also H.R. Rep. No. 735, 86th Cong., 1st Sess. 5 (1959); S. Rep. No. 1182, 85th Cong., 2d Sess. 2 (1958).¹¹

¹¹ 26 U.S.C. 7215(a) provides that any person who fails to comply with the withholding requirements, after receipt of notice of these requirements pursuant to 26 U.S.C. 7512(b), is guilty of a misdemeanor punishable by a maximum fine of \$5,000 or a maximum prison term of one year, or both. See, e.g., *United States v. McMullen*, 516 F.2d 917, 920 (C.A. 7); *United States v. Patterson*, 465 F.2d 360, 361 (C.A. 9), certiorari denied, 409 U.S. 1038. See also 8A Mertens, *Law of Federal Income Taxation*, § 47A.25a, pp. 216-222 (1971 rev.).

See also 26 U.S.C. 7202, which provides that willful failure

Despite the enactment of the criminal statute, the Treasury continued to press for non-dischargeability in bankruptcy of the responsible officer's obligation to pay withholding taxes in order to enhance the collectability of such taxes, which "shall be held to be a special fund in trust for the United States" (26 U.S.C. 7501): As David A. Lindsay, the Assistant to the Secretary, wrote to Representative Celler, the Chairman of the House Committee on the Judiciary, the criminal provisions would not be effective in eliminating delinquencies in trust fund taxes arising prior to the Internal Revenue Service's issuance of a special notice to the responsible person. "These delinquencies simply become a part of the unpaid tax liability of the bankrupt, and the problem which exists upon the failure of the bankrupt to keep these trust fund moneys intact remains in spite of the passage of * * * [the criminal statute]." H.R. Rep. No. 735, *supra*, at 7.

The Treasury's practical experience confirmed the accuracy of its earlier prediction that the criminal provision would not be effective in preventing delinquencies in trust fund tax liabilities. In 1961, Assistant Secretary of the Treasury Stanley S. Surrey wrote to Senator Eastland, the Chairman of the Senate Committee on the Judiciary: "Delinquency in this area has increased in recent years, and the Department considers it most undesirable to permit

to collect and pay over taxes is a felony punishable by a maximum fine of \$10,000 or a maximum prison term of five years, or both.

persons who are charged with the responsibility of paying over to the Federal Government moneys collected from third persons to be relieved of their obligations in bankruptcy when they have converted such moneys for their own use." S. Rep. No. 114, 89th Cong., 1st Sess. 10 (1965). See also H.R. Rep. No. 372, 88th Cong., 1st Sess. 6 (1963).

In response to this repeatedly stated concern of the Treasury that the personal bankruptcy of a responsible officer such as respondent would serve as a shield against his Section 6672 liability for unpaid withholding taxes, Congress added subsection (e) to Section 17a(1) of the Bankruptcy Act. It provides: "That a discharge in bankruptcy shall not release a bankrupt from any taxes * * * (e) which the bankrupt has collected or withheld from others as required by the laws of the United States * * *, but has not paid over * * *." As the House Committee explained in reporting out "the measure, the purpose of the amendment was "to exempt from the provisions of this bill taxes which the bankrupt has collected or withheld from others under Federal or State law." H.R. Rep. No. 372, *supra*, at 1. In the House Committee's view, "* * * the objection of Treasury to the discharge of so-called trust fund taxes has been met by the amendment to this bill." *Id.* at 5. The Senate Reports likewise confirm that the purpose of Section 17a(1) (e) was to render trust fund taxes non-dischargeable in bankruptcy. S. Rep. No. 1134, 88th Cong., 2d Sess. 1, 6 (1964); S. Rep. No. 114, *supra*, at 6.

2. In light of the foregoing legislative history, there is no basis for the court of appeals' conclusion (Pet. App. C, p. 21a) that Section 17a(1)(e) applies only to the corporate employer and not to the Section 6672 liability of the officer responsible for the collection and payment of withheld taxes. In the court of appeals' view (*ibid.*), Section 17a(1)(e) of the Bankruptcy Act "applies only to taxes 'which the bankrupt has collected or withheld from others as required by the laws of the United States,' and it was not Sotelo himself, but his employer-corporation, that was obligated by law to collect and withhold the taxes governed by the proviso."

But the court's restrictive gloss on Section 17a(1) (e) cannot be squared with the fact that respondent was a "person required to collect, truthfully account for, and pay over" his corporation's withholding taxes under Section 6671(b) and 6672 of the Code. These statutory provisions recognize that corporations are inanimate legal entities that can act only through their officers or employees. While the corporation was obligated to collect and pay over these taxes, that function was statutorily required to be performed by respondent himself.

Respondent "collected" such taxes by paying net wages to his employees. However, he willfully failed to pay them over to the government. Thus, respondent is a "bankrupt [who] has collected or withheld [taxes] from others as required by the laws of the United States * * * but [who] has not paid [them] over" within the meaning of Section 17a(1)(e).

Moreover, the court's reading of Section 17a(1)(e) ignores the explicitly stated congressional intent to preserve the liability for trust fund taxes beyond the bankruptcy of persons responsible for the collection and payment of withholding taxes. Indeed, there would have been little reason for Congress to render non-dischargeable the corporate employer's obligations to pay withholding taxes, since it was fully aware that for all practical purposes a corporation effectively ceases to exist after a liquidating bankruptcy. As both the House and Senate Committee reports observed, "Although a corporate bankrupt is theoretically not discharged, the corporation normally ceases to exist upon bankruptcy and unsatisfied tax claims, as well as all other unsatisfied claims, are without further recourse even though the enterprise may continue in a new corporate form." H.R. Rep. No. 735, *supra*, at 2; S. Rep. No. 114, *supra*, at 2-3. In providing for the non-dischargeability of "taxes * * * which the bankrupt has collected or withheld from others as required by the laws of the United States * * *," Congress intended to protect the revenues by providing that the obligation to pay over such taxes that Sections 6671(b) and 6672 impose upon a corporate officer such as respondent should survive his personal bankruptcy.¹²

¹² See Kennedy, *The Bankruptcy Amendments of 1966*, 1 Ga. L. Rev. 149, 177 (1967); Marsh, *Triumph or Tragedy? The Bankruptcy Act Amendments of 1966*, 42 Wash. L. Rev. 681, 694 (1967).

The court of appeals' further conclusion that Section 17a(1)(e) is inapplicable because it "renders only 'taxes' nondischargeable, not a 'penalty' imposed under 26 U.S.C. § 6672" (Pet. App. C, p. 21a), is equally erroneous. As we shall argue in Part C, *infra*, pp. 25-32, the liability equal to unpaid withholding taxes that is imposed by Section 6672 upon a responsible officer is a non-dischargeable tax within the meaning of Section 17a(1) and not a dischargeable compensatory penalty. But whether or not respondent's personal liability for the unpaid withholding taxes is a "tax" or a "penalty," the phrase "taxes * * * which the bankrupt has collected or withheld from others" in Section 17a(1)(e) encompasses the sums at issue here.

The structure of the statute—with the phrase "collected or withheld from others" modifying the word "taxes"—confirms that the amounts at issue must be characterized at the time of collection or withholding. At the time respondent collected or withheld funds from the wages of his corporation's employees, those funds were "taxes" and not penalties. Respondent's subsequent willful failure to pay the amounts withheld over to the government, which triggered his liability under Section 6672, did not change their essential character as taxes for purposes of Section 17a(1)(e).¹³

¹³ Currently pending bankruptcy legislation (H.R. 8200, 95th Cong., 1st Sess. (1977)) excepts Section 6672 liability from discharge. The bill provides (proposed 11 U.S.C. 523(a)(1)) that a discharge under the title does not discharge

3. The court of appeals attempted to buttress its decision with the observation that "[a]s a policy matter, the government's position that [respondent] remains personally liable, notwithstanding bankruptcy, for taxes required to be withheld by his corporation, can lead to substantial inequities" (Pet. App. C, *infra*, p. 21a). In the court's view, there is

an individual debtor from any debt—"for a tax—(A) of the kind and for the periods specified in section 507(6)." Section 507(6) (C) specifies that "taxes required to be withheld from wages, salaries, commissions, dividends, interest, or other payments that were paid by the debtor, or by a corporation or partnership that is an insider if the debtor is liable for such taxes * * *" are included in the category of taxes to be accorded priority, and by virtue of the reference in Section 523(a) (1), the liability for such taxes is rendered nondischargeable. The term "insider" includes officers, directors and persons in control of the corporations (see proposed 11 U.S.C. 101(24)). See also, Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 93-137, Part II, 93d Cong., 1st Sess. 110, 116, 136 (1973).

In reporting out this measure, the House Committee viewed the bill as consistent with present law. The House Report stated (H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 191 (1977)):

The current Bankruptcy Act renders nondischargeable all taxes which the bankrupt has collected or withheld from others but has not paid over. Thus, withholding taxes are accorded an unlimited priority under present law. The priority even includes the 100 percent "penalty" imposed under the Internal Revenue Code. The present unlimited priority is justified by the notion that withholding taxes are held in trust. [Footnotes omitted.]

Compare *id.* at 190, with the comments of Representative Edwards, 123 Cong. Rec. H11708-H11709 (daily ed., October 27, 1977). See also Senate Bill 2266, 95th Cong., 1st Sess. (1977), which would also continue the non-dischargeability of the Section 6672 liability.

no nexus between the estate of an individual bankrupt corporate officer and the liability of his corporation for unpaid withholding taxes.

But Section 6672 creates the nexus that the court believed to be lacking by imposing personal liability for such taxes upon the officer whose preference of other creditors over the government benefitted his corporation in the first instance. There is no inequity in providing that the corporate officer whose actions resulted in the corporation's withholding tax delinquency cannot eliminate his liability for such taxes through personal bankruptcy.

Indeed, contrary to the assumption of the court of appeals, its decision subjects the government to a substantial inequity. By failing to pay the taxes withheld from his employees' wages, respondent wrongfully appropriated moneys and contributed them to the capital of his corporation despite the statutory command that such amounts "shall be held to be a special fund in trust for the United States" (26 U.S.C. 7501).

As we have pointed out *supra*, p. 11, the government credits the employees' accounts with the taxes withheld despite the willful failure of a corporate officer such as respondent to pay them over to the government. In such circumstances, the government obligates itself to pay social security benefits and income tax refunds to the employees even though it has not received the necessary taxes. If, as the decision below holds, the responsible officer can violate his fiduciary obligation to the government and thereafter shield himself from liability by means of

personal bankruptcy," the government potentially stands to suffer a twofold loss—first, by failing to receive taxes that are lawfully due, and second, by disbursing benefits on the assumption that the taxes necessary to fund those benefits have been paid.

Finally, the court of appeals thought that the result we seek in this case would "contravene the Bankruptcy Act's basic policy of settling a bankrupt's past debts and providing a fresh economic start" (Pet. App. C, p. 22a). However, these general considerations do not answer the specific statutory question at bar whether the liability imposed by Section 6672 is dischargeable under Section 17. The latter provision sets forth a detailed list of classes of obligations that Congress determined as a matter of policy were not properly dischargeable in bankruptcy.

As this Court stated in *Bruning v. United States*, 376 U.S. 358, 361, in terms that are equally appropriate here: "Nor is petitioner aided by the now-familiar principle that one main purpose of the Bankruptcy Act is to let the honest debtor begin his financial life anew. * * * § 17 is not a compassionate section for debtors. Rather, it demonstrates congressional judgment that certain problems—*e.g.*, those of financing government—override the value of giving the debtor a wholly fresh start" (footnote omitted).

¹⁴ Compare Section 17a(4) of the Bankruptcy Act, which bars a discharge of obligations that "were created by [a bankrupt's] fraud, embezzlement, misappropriation or defalcation while acting as an officer or in any fiduciary capacity."

If the Court agrees with the foregoing submission that respondent's withholding tax liability is non-dischargeable under Section 17a(1)(e), it need not reach our alternative argument, *infra*, pp. 25-32, that the liability is a non-dischargeable "tax" under Section 17a(1). However, since the conflict in the circuits concerns that alternative statutory ground (see Pet. 5-7, 11-12), the Court may wish to address the point in the interest of the orderly administration of the internal revenue and bankruptcy laws. See *Donaldson v. United States*, 400 U.S. 517, 531-536.

C. The Liability For Unpaid Withholding Taxes Imposed Upon A Responsible Officer By Section 6672 Is A Non-Dischargeable Tax Under Section 17a(1) Of The Bankruptcy Act

1. Section 17a of the Bankruptcy Act provides that—

A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as (1) are taxes which became legally due and owing by the bankrupt to the United States * * * within three years preceding bankruptcy.

If, as we submit, respondent's liability for his corporation's unpaid withholding taxes is a tax, Section 17a(1) offers an independent ground for the non-dischargeability of the government's claim against respondent.¹⁵

¹⁵ The three-year limitations period does not bar the government's claim in this case because the withholding taxes

Despite the "penalty" nomenclature employed by Section 6672 in describing the responsible officer's liability for unpaid withholding taxes (see *infra*, pp. 29-32), the authorities have always regarded that liability as a tax. There is accordingly no sound reason for the court of appeals' conclusion that the Section 6672 liability is a dischargeable compensatory penalty rather than a non-dischargeable tax.¹⁶ As a historical

at issue were due to be paid in 1971 and 1973, and respondent filed his petition in bankruptcy on July 5, 1973 (Pet. App. A, p. 1a). The legislative history of Section 17a(1) indicates that the phrase "due and owing" means the date on which the return is due to be filed and the taxes paid. See comments of Senator Ervin, 112 Cong. Rec. 13814 (1966); see also, comments of Senator Gore, 112 Cong. Rec. 13812-13813 (1966). See also Internal Revenue Manual, Part V, par. 5922.2(5); 1A *Collier on Bankruptcy* ¶ 17.14[1] (14th ed.). The liability for taxes under Section 6672 is deemed to be "due and owing" on the date the person responsible for seeing that the taxes are paid failed to do so—the date the corporate returns were due to be filed. Under 26 U.S.C. 6501(b)(2), the quarterly withholding tax returns are deemed to be filed on April 15 of the succeeding calendar year.

¹⁶ In holding that the liability imposed by Section 6672 is a "penalty" rather than a "tax," the court of appeals did not distinguish between a non-compensatory and a compensatory penalty. If the court had classified the Section 6672 liability as a non-compensatory penalty, presumably it would have held that the liability was non-dischargeable. Because the purpose of such a penalty is to punish the bankrupt rather than his creditors, penalties are not allowable out of the assets of the bankruptcy estate and are non-dischargeable. See 1A *Collier on Bankruptcy*, *supra*, at ¶¶ 1705, 17.13; Bankruptcy Act, Section 57j, 30 Stat. 561, as amended (11 U.S.C. 93(j)); *Simonson v. Granquist*, 369 U.S. 38. However, compensatory penalties are allowable under Section 57j of the Bankruptcy Act and, as such, are presumptively discharge-

matter, Congress has always excepted all federal taxes from discharge in bankruptcy¹⁷ and has accorded federal taxes priority over other creditors' claims. See Section 64a(4), 11 U.S.C. 104(a)(4). Since Section 6672 is a device to collect what are indisputably taxes, the liability it imposes upon persons such as respondent who are responsible for their collection and payment is likewise a non-dischargeable "tax" within the meaning of Section 17a(1). Indeed, Section 6672 does not impose a penalty but simply shifts the tax obligation from the business entity to the responsible officer without any further economic sanction that could be deemed to be a fine.¹⁸ Respondent's liability under Section 6672 is no less a tax liability because his corporation was also liable for the taxes.

The foregoing analysis finds support in the decisions of this Court defining the term "tax" as used in the Bankruptcy Act. As the Court has observed, the term "tax" in that statutory context is "a pecuniary burden laid upon individuals or property for the purpose of supporting the Government" (*New*

able. 2 Remington on *Bankruptcy*, § 3304 (6th ed.). We therefore assume that the court intended to hold that the liability was a compensatory penalty.

¹⁷ The three-year limitations period was added to the statute in 1966 to eliminate stale tax claims. See H.R. Rep. No. 735, *supra*, at 2-3; S. Rep. No. 114, *supra*, at 2-3.

¹⁸ In analogous circumstances, Sections 6901 and 2002 of the Code impose liability for taxes upon transferees and executors of estates, which are not penalties dischargeable in bankruptcy but non-dischargeable taxes. *Hamar v. Commissioner*, 42 T.C. 867, 878-879.

Jersey v. Anderson, 203 U.S. 483, 492) "by whatever name it may be called" (*United States v. New York*, 315 U.S. 510, 515-516). See also *Sonzinsky v. United States*, 300 U.S. 506, 513; *Bob Jones University v. Simon*, 416 U.S. 725, 741; *United States v. Butler*, 297 U.S. 1, 61. Moreover, the Section 6672 liability "is not any the less a tax laid on * * * [respondent] because the statute places a like burden in the alternative on the * * * [corporation] * * *." *New York v. Feiring*, 313 U.S. 283, 287.

Put another way, respondent cannot exploit his willful failure to collect and pay over the withholding taxes—the fact upon which his personal liability rests—as a ground for recharacterizing his statutory obligation to pay such taxes. Since Section 6672 does not seek to punish the responsible officer but only to collect corporate withholding tax delinquencies for the purpose of supporting the government, it is a non-dischargeable "tax" within the meaning of Sec-

¹¹ Section 6672 applies where the responsible person "willfully" fails to pay over the required taxes. The statutory term "willful" as used in the section refers only to a voluntary and conscious decision to prefer other creditors. *Harrington v. United States*, 504 F.2d 1306 (C.A. 1); *Horwitz v. United States*, 339 F.2d 877, 878 (C.A. 2); *Liddon v. United States*, 448 F.2d 509, 513 (C.A. 5), certiorari denied, 406 U.S. 918; *Braden v. United States*, 442 F.2d 342 (C.A. 6), certiorari denied *sub nom.* *Bonistall v. Braden*, 404 U.S. 912; *Monday v. United States*, 421 F.2d 1210, 1215-1216 (C.A. 7), certiorari denied, 400 U.S. 821; *United States v. Strebler*, 313 F.2d 402, 405 (C.A. 8); *Teel v. United States*, 529 F.2d 903, 905 (C.A. 9); *Burden v. United States*, 486 F.2d 302, 304 (C.A. 10), certiorari denied, 416 U.S. 904.

tion 17a(1) and not a penalty. Cf. *United States v. Childs*, 266 U.S. 304, 307.

2. In holding that respondent's Section 6672 liability was a dischargeable compensatory "penalty" rather than a non-dischargeable obligation for "taxes * * * legally due and owing by the bankrupt to the United States," the court of appeals relied upon the use of the word "penalty" in Section 6672 to describe a corporate officer's personal obligation for unpaid taxes withheld from the corporation's employees. Pursuant to that provision, a responsible officer who willfully fails to pay over the tax "shall * * * be liable to a *penalty* equal to the total amount of the tax evaded, or not collected * * *." As the court viewed the matter, its conclusion was required by "Congress' own characterization of the liability it created in Section 6672" (Pet. App. C, p. 20a).

But as we have pointed out *supra*, pp. 11-12, 26-28, Section 6672 does not impose a "penalty" in the usual sense of that term; it simply shifts the withholding tax liability from the corporation to the responsible officer when the officer willfully fails to pay over the taxes to the government. Indeed, it is the longstanding policy of the Internal Revenue Service to assert Section 6672 liability against a responsible officer only when, as here, the corporate employer is unable to pay the withholding taxes. Moreover, the amount of the Section 6672 liability is collected only once. Thus, when the Service makes more than one assessment of Section 6672 liability against several officers responsible for a single default, a payment of some part of

the tax results in a *pro tanto* abatement of the assessments. See Policy Statement P-5-60 (Approved November 5, 1956) MT 1218-56; U.S. Comp. Gen. Op. B-137762, May 3, 1977 (9 CCH Standard Fed. Tax Rep., ¶ 6614, p. 71,438 (1977)). See also *Hartman v. United States*, *supra*, 538 F.2d at 1340; *Newsome v. United States*, *supra*, 431 F.2d at 746.²⁰

Since the Treasury has always administered Section 6672 as a method to collect what are undisputably taxes, the courts of appeals (except for the decisions below) and the Court of Claims have uniformly recognized that "[i]ts basic purpose is the protection of governmental revenue" "[d]espite its denomination as a 'penalty' assessment * * *." *Monday v. United States*, *supra*, 421 F.2d at 1216. Accord: *Harrington v. United States*, *supra*, 504 F.2d at 1311; *Spivak v. United States*, 370 F.2d 612, 616 (C.A. 2), certiorari denied, 387 U.S. 908; *Cross v. United States*, 311 F.2d 90, 94 (C.A. 4); *Moore v. United States*, 465 F.2d 514, 517 (C.A. 5), certiorari denied, 409 U.S. 1108; *Mueller v. Nixon*, *supra*, 470 F.2d at 1350; *Sorenson v. United States*, 521 F.2d 325,

²⁰ But cf. *Otte v. United States*, 419 U.S. 43, 52. There, in dictum, the Court described the Section 6672 liability as "a penalty, apart from the tax, on a person who willfully fails to fulfill his obligation to withhold * * *." That case, however, dealt with the priority of withholding taxes on wages paid during bankruptcy and did not involve the imposition of the Section 6672 liability. Thus, none of the considerations discussed above in the text as to how the statute is administered and is characterized by the case law were brought to the attention of the Court in *Otte*.

328 (C.A. 9); *White v. United States*, 372 F.2d 513, 516 (Ct. Cl.).²¹

It is therefore hardly surprising that prior to the decision below, two circuits (*Murphy v. Internal Revenue Service*, 533 F.2d 941 (C.A. 5), affirming 381 F. Supp. 813, 816-817 (N.D. Ala.); *Lackey v. United States*, 538 F.2d 592 (C.A. 4)), as well as every reported district court decision, regarded it as settled that the liability imposed by Section 6672 is a non-dischargeable tax under Section 17a(1) of the Bankruptcy Act because it "is not a penalty as that term is generally used, but in reality is a liability for a tax originally imposed upon the corporation and shifted to the corporate officer upon his default." *Sherwood v. United States*, 228 F. Supp. 247, 251

²¹ See also *Botta v. Scanlon*, 314 F.2d 392 (C.A. 2), holding that the liability imposed by Section 6672 is a "tax," the collection of which cannot be enjoined because of the Anti-Injunction Act, 26 U.S.C. 7421(a). The court of appeals sought to distinguish that case on the ground that Section 6671(a) provides that the Section 6672 liability is to be regarded as a "tax" for purposes of the Internal Revenue Code and that there is no similar provision in the Bankruptcy Act (see Pet. App. C, pp. 19a-20a).

But it does not follow that, because there is no statutory equivalent of Section 6671(a) in the Bankruptcy Act, the liability must be regarded as a penalty under that Act. Whether the liability is a tax for purposes of the Bankruptcy Act depends upon the meaning of the term "tax" as it is used in the Bankruptcy Act. As we have pointed out *supra*, pp. 27-28, the decisions of this Court have established that the term "tax" is broadly used by the Bankruptcy Act to mean a pecuniary burden laid upon individuals or property for the purpose of supporting the government.

(E.D. N.Y.). Accord: *Severance v. United States*, 76-2 U.S.T.C., par. 9643, pp. 85,026-85,027, decided June 3, 1976 (N.D. Tex.); *Westenberg v. United States*, 285 F. Supp. 915, 917 (D. Ariz.); *Lynn v. Scanlon*, 234 F. Supp. 140, 144-145 (E.D. N.Y.).²² The standard bankruptcy and tax treatises and commentators likewise agree that the liability is a non-dischargeable tax. 1A Collier on *Bankruptcy*, ¶ 17.14 [9] n. 38 (14th ed.); 8 Remington on *Bankruptcy*, § 3317 (1976 Supp., 6th ed.); 8A Mertens, *Law of Federal Income Taxation*, § 47A.25a, p. 209 (Rev. 1971); see also Kingsmill, *When and How is a Bankrupt Discharged from Federal Tax Debt*, 31 J. Tax. 180, 182 (1969).

²² See also *Kalb v. United States*, *supra*, 505 F.2d at 509; *Larson v. United States*, 340 F. Supp. 1197, 1199 (E.D. Wis.); *Matter of Baker*, 73-1 U.S.T.C., par. 9406, p. 80,958, decided March 6, 1973 (W.D. Pa.); *Butler v. Cohen*, 69-2 U.S.T.C., par. 9466, p. 85,112 n. 6, decided May 13, 1969 (N.D. N.Y.); *In re O'Fall*, 368 F. Supp. 345, 349, 351 (D. Kan.). Contra: *United States v. Young*, E.D. Wis., No. 70-C-332, decided August 26, 1977, where the court was required to follow the Seventh Circuit's decision in this case.

CONCLUSION

The judgment of the court of appeals should be reversed.²³

Respectfully submitted.

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NOVEMBER 1977.

²³ The government failed to point out to the court of appeals that the questions of dischargeability of respondent's Section 6672 liability and the right to the homestead fund were independent. Thus, in holding respondent Onofre Sotelo's Section 6672 liability to be dischargeable, the court of appeals erroneously assumed that it did not have to reach the alternative argument, rejected by the bankruptcy judge (Pet. App. A, pp. 7a-10a), that his wife was entitled to a state homestead exemption free from her husband's liability (see Pet. App. C, p. 22a n. 3). However, whether or not Onofre Sotelo's liability is dischargeable, the court of appeals must at all events address the contention that his wife owned the \$10,000 homestead fund (see *supra*, pp. 4-5). Since that fund was set apart outside the bankruptcy estate and levied upon by the Internal Revenue Service, it was not property acquired after bankruptcy that would be affected by a discharge. With respect to such property, Section 541(1) provides that "a discharge shall not be a bar to any remedies available under applicable law to the United States or to any State or any subdivision thereof,

against the exemption of the bankrupt allowed by law and duly set apart to him under this title * * *." See 1A Collier on *Bankruptcy*, *supra* ¶ 17.14[7]. Under 26 U.S.C. 6334(a) and (c), the homestead fund is not exempt from a federal tax levy. The government's claim to that fund can only be defeated if Naomi Sotelo is deemed to have owned the homestead.

Thus, the question of dischargeability is irrelevant to the government's right to the homestead fund. However, the parties also put at issue in the lower courts the dischargeability of the government's tax claim of \$32,840.71. The court of appeals decided the case on that issue, and that is the question presented in the petition (p. 2).

APPENDIX A*

Internal Revenue Code of 1954 (26 U.S.C. (1970 ed., as amended by the Tax Reform Act of 1976, Pub. L. 94-455, 90 Stat. 1520, 1557)):

SEC. 3101 [as amended by Section 321(b), Social Security Amendments of 1965, 79 Stat. 395.] RATE OF TAX.

(a) Old-Age, Survivors, and Disability Insurance.—In addition to other taxes, there is hereby imposed on the income of every individual a tax equal to the following percentages of the wages (as defined in section 3121(a)) received by him with respect to employment (as defined in section 3121(b))—

SEC. 3102. DEDUCTION OF TAX FROM WAGES.

(a) [as amended by Section 205, Social Security Amendments of 1954, 68 Stat. 1093; Section (h)(3), Social Security Amendments of 1956, 70 Stat. 841; and Section 313(c)(2), Social Security Amendments of 1965, 79 Stat. 383]. Requirement.—The tax imposed by section 3101 shall be collected by the employer of the taxpayer, by deducting the amount of the tax from the wages as and when paid. An employer who in any calendar quarter pays to an employee cash remuneration to which paragraph (7)(B) or (C) or (10) of section 3121(a) is applicable may deduct an amount equivalent to such tax

* There is no material difference between the current statutory provisions and those which existed during the years at issue. We are therefore setting forth in this Appendix the current statutory provisions.

from any such payment of remuneration, even though at the time of payment the total amount of such remuneration paid to the employee by the employer in the calendar year is less than \$50; and an employer who in any calendar year pays to an employee cash remuneration to which paragraph (8)(B) of section 3121(a) is applicable may deduct an amount equivalent to such tax from any such payment of remuneration, even though at the time of payment the total amount of such remuneration paid to the employee by the employer in the calendar year is less than \$150 and the employee has not performed agricultural labor for the employer on 20 days or more in the calendar year for cash remuneration computed on a time basis; and an employer who is furnished by an employee a written statement of tips (received in a calendar month) pursuant to section 6053(a) to which paragraph 12(B) of section 3121(a) is applicable may deduct an amount equivalent to such tax with respect to such tips from any wages of the employee (exclusive of tips) under his control, even though at the time such statement is furnished the total amount of the tips included in statements furnished to the employer as having been received by the employee in such calendar month in the course of his employment by such employer is less than \$20.

(b) Indemnification of Employer.—Every employer required so to deduct the tax shall be liable for the payment of such tax, and shall be indemnified against the claims and demands of any person for the amount of such payment made by such employer.

• • • • •
SEC. 3402. INCOME TAX COLLECTED AT SOURCE.

(a) [as amended by Section 401(d). Tax Reform Act of 1976, 90 Stat. 1557]. Requirement of Withholding.—Except as otherwise provided in this section, every employer making payment of wages shall deduct and withhold upon such wages a tax determined in accordance with tables prescribed by the Secretary. With respect to wages paid prior to January 1, 1978, the tables so prescribed shall be the same as the tables prescribed under this section which were in effect on January 1, 1976. With respect to wages paid after December 31, 1977, the Secretary shall prescribe new tables which shall be the same as the tables proscribed under this subsection which were in effect on January 1, 1975, except that such tables shall be modified to the extent necessary to reflect the amendments made to subsections (b) and (c) of Section 141 by the Tax Reform Act of 1976. For purposes of applying such tables, the term "the amount of wages" means the amount by which the wages exceed the number of withholding exemptions claimed, multiplied by the amount of one such exemption as shown in the table in subsection (b)(1).

• • • • •
SEC. 3403. LIABILITY FOR TAX.

The employer shall be liable for the payment of the tax required to be deducted and withheld under this chapter, and shall not be liable to any person for the amount of any such payment.

SEC. 6671. RULES FOR APPLICATION OF ASSESSABLE PENALTIES.

(a) *Penalty Assessed as Tax.*—The penalties and liabilities provided by this subchapter shall be paid upon notice and demand by the Secretary or his delegate, and shall be assessed and collected in the same manner as taxes. Except as otherwise provided, any reference in this title to “tax” imposed by this title shall be deemed also to refer to the penalties and liabilities provided by this subchapter.

(b) *Person Defined.*—The term “person”, as used in this subchapter, includes an officer or employee of a corporation, or a member or employee of a partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs.

SEC. 6672. FAILURE TO COLLECT AND PAY OVER TAX, OR ATTEMPT TO EVADE OR DEFEAT TAX.

Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over. No penalty shall be imposed under section 6653 for any offense to which this section is applicable.

SEC. 7501. LIABILITY FOR TAXES WITHHELD OR COLLECTED.

(a) *General Rule.*—Whenever any person is required to collect or withhold any internal revenue tax from any other person and to pay over such tax to the United States, the amount of tax so collected or withheld shall be held to be a special fund in trust for the United States. The amount of such fund shall be assessed, collected, and paid in the same manner and subject to the same provisions and limitations (including penalties) as are applicable with respect to the taxes from which such fund arose.

* * * *

Bankruptcy Act, c. 541, 30 Stat. 544, 550, Sec. 17 [as amended by Sec. 1, Act of June 22, 1938, c. 575, 52 Stat. 840, 851] (11 U.S.C. 35):

SEC. 17. *Debts not affected by a discharge.*

a [as amended by Section 2, Act of July 5, 1966, Pub.L. 89-496, 80 Stat. 270]. A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as (1) are taxes which became legally due and owing by the bankrupt to the United States or to any State or any subdivision thereof within three years preceding bankruptcy: *Provided, however,* That a discharge in bankruptcy shall not release a bankrupt from any taxes (a) which were not assessed in any case in which the bankrupt failed to make a return required by law, (b) which were assessed within one year preceding bankruptcy in any

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ROCK IS., CLERK J. P. O. Box 12 105 Seaside			<div style="float: right; text-align: right;">754 1-1-73-223</div> <div style="clear: both;"></div> <div style="float: left; width: 40%;"> <p>DATE RECEIVED 7-5-73</p> <p>CITY AND COUNTY Alpha Henry Illinois</p> <p>NAME OF AGENT Robert D. Morgan Stanley J. Covey</p> </div> <div style="float: right; width: 55%;"> <p>RECEIVED BY CLERK</p> <p>DATE 7-5-73</p> <p>TIME 10:00 AM</p> <p>BY CLERK</p> <p>REMARKS CLERK'S FEE</p> </div>		
DATE	DESCRIPTION	RECEIVED	DISBURSED	BALANCE	
July 5	Winstein, Kavensky & Wallace	55.00			
July 9	Tr. U. S. Ref. Sal. & Exp. CD#1		37.00		
July 9	Tr. U. S. Clerk's Fee CD#1		1.00	15.00	
July 25	Winstein, Kavensky & Wallace Amend.	10.00			
July 30	Tr. Ref. Sal. CD#4		10.00		
August 6	Viola Masgrave, Ct. Rep. Vo #5 Check # 14752		5.00	10.00	
August 20	Waldo M. Wissler Reel.	10.00			
August 20	Tr. U.S.Ref. Sal. & Exp. CD#9		10.00		
Oct. 19	Winstein, Kavensky & Wallace Amend.	10.00			
Oct. 23	Tr. U. S. Ref. Sal.&Exp. CD#16		10.00		
1976					
Feb. 5	Bruce L. Balch, Notice of Appeal Record filed with Clerk 2-4-76	10.00			
Feb. 9	Tr.U.S.Ref.Sal.&Exp. CD#19-RI		10.00		
Mar.22	Bruce L. Balch, Notice of Appeal TR. U.S.Treas. Clerk's Fee CD#23	5.00			
Mar. 22	Bond for cost on Appeal Dep. Reg. Fund CD#17-RI	\$250.00			
			\$250.00		

Feb. 2 Notice of Appeal to District Court filed by bankrupts.
Feb. 2 Designation and Issues on Appeal filed.
Feb. 4 Record on Appeal filed with clerk of U. S. District Court
on this date. Attorneys of record notified by Clerk
of docketing date. (Record forwarded to Judge Morgan)

Feb. 23 Decision and Order filed and entered wherein it is Ordered
that the Order of the Bankruptcy Judge herein filed
January 23, 1976 is AFFIRMED on appeal in this Court.
(See Decision and Order) (Morgan, J.) (Copies of
Decision and Order mailed to Attorneys of Record by
the Court.) (Record on Appeal returned to BK. Court)

Mar. 22 Notice of Appeal filed by Osofre J. and Naomi Sotelo.
(Copy of Notice of Appeal and Clerk's docket entries
mailed to U. S. Court of Appeals on 3-24-76. U.S. Atty.
and Trustee notified by Clerk.) Bond on Appeal filed. CDS17-RI.

Mar. 24 Record on Appeal returned to Clerk from Bankruptcy Court.

Apr. 28 Original Record on Appeal forwarded to the U. S. Court
of Appeals for the 7th Circuit along with Clerk's
Certification. (Copy of record mailed to Atty. Balch.)

Contract No.

76-34

<input type="checkbox"/> Civil Admin. Review <input type="checkbox"/> U.S. Civil Admin. Enforcement <input type="checkbox"/> Tax Court Bankruptcy <input type="checkbox"/> Orig. Prison Criminal	District <u>S. 111., RI Div.</u> Filed in U. C. <u>11-5-73</u> Number <u>RI-DK-73-233 add 334</u> Notice of Appeal <u>3-22-76</u> Judge <u>Morgan</u>			Federal Prisoner <input type="checkbox"/> State Prisoner <input type="checkbox"/> Type Petition _____
Title: <u>IN THE MATTERS OF:</u> <u>ONOFRE J. SOTELLO and NAOMI SOTELLO,</u> <u>Bankrupts-Appellants.</u>				
Appearance Attorney(s) For Appellant(s) (Appointed On _____) Address _____				
<u>6/23/76</u> <u>Bruce L. Balch, 402 1st Natl. Bk. Bldg., P.O. Box 66, Rock Twn,</u> <u>IL 61201</u>				
Appearance Attorney(s) For Appellee(s) (Appointed On _____) Address _____				
<u>5/22/76</u> <u>Donald B. Mackay, P.O. Box 375 Springfield, IL 62705</u> <u>5/22/76</u> <u>Robert J. Rauffman, P.O. Box 209, Peoria, IL 61601</u> <u>5/24/76</u> <u>Scott P. Crampton, Asst. Atty. Gen., Tax Div., D/J. Wash. DC20530</u> <u>5/24/76</u> <u>Gilbert E. Andrews, Chief Appellate Section</u>				
(OVER) Contents of Record Filed <u>5-3-76</u> Supplemental Records _____ Filings: <u>one</u> volumes. Date _____ Contents _____ Transcripts: _____ volumes. _____ Depositions: _____ volumes. _____ Exhibits: _____ Other: _____				
Miscellaneous What Withdrawn Date By Whom By Court				
<u>Idgs., tape</u> <u>1/20/77</u> <u>L.C.</u> _____				
Summary Of Events Briefs Distributed: <u>CDV 0 - 173</u> Date of Oral Arg: <u>12/3/76</u> Panel: <u>J. Bauer, J. Wood, J. Grant</u> Opinion Date: <u>3/24/77 Bauer</u> Order Dated: _____ Disposition: <u>REVERSED & REPENDS</u> Reported At: <u>551</u> <u>1095</u> Petition For Rehearing: _____ Granted <input type="checkbox"/> Denied <input type="checkbox"/> Mandate Issued: <u>4/15/77</u> Rev. and Withdrawn: <u>4/15/77</u>				
Docketed: <u>5-3-76</u> Docket Fee Paid: <u>5-3-76</u> In Forma Pauperis <input type="checkbox"/> Appendix: _____ Appellant's Brief: <u>6/30/76</u> Appellant's Brief: _____ Appellee's Brief: <u>8/2/76</u> Appellee's Brief: _____ C.R. 77: <input type="checkbox"/> Granted <input type="checkbox"/> Denied <input type="checkbox"/> All 7 Copies _____ Reply Brief: <u>8/23/76</u> _____ Brief: _____ Additional Authority _____ Notice of Oral Arg: <u>3/12/76</u>				

UNITED STATES COURT OF APPEALS
SEVENTH CIRCUIT

Docket 76-14

DATE	FILINGS-PROCEEDINGS
6/29/76	Filed 0&3c of appellants motion for ext. of time to file brief and aff.
6/30/76	Entered order that the Clerk file instant the 25c of appellants brief.
6/30/76	Filed 25c of appellant's brief, per order—svc.
8/2/76	Filed 15c of appellee's brief—svc.
8/9/76	Filed 0 & 3c appellants' motion for extension of time to file reply brief.
8/10/76	Entered Order extending time for appellants' to file brief to 8/26/76.
8/23/76	Filed 15c appellants reply brief—svc.
10/12/76	Entered order setting appeal for oral argument on 12/3/76; 9:30. Oral argument limited to 15 min. per/side
12/3/76	Heard and taken under advisement.
3/24/77	Filed opinion by Judge Bauer.
3/24/77	Entered final judgment order, REVERSING, with costs, and REMANDING.
4/15/77	MANDATE ISSUED
4/20/77	Filed receipt from district court for mandate and record.
6/23/77	Filed notice of filing petition for cert. on 6/17/77. Supreme Ct. 76-1800.

IN THE DISTRICT COURT
OF THE UNITED STATES
FOR THE SOUTHERN DISTRICT OF ILLINOIS
NORTHERN DIVISION

RI-BK-73-233/234

MERGED CASES

IN THE MATTER OF

ONOFRE J. SOTELO and NAOMI SOTELO,
BANKRUPTS

NOTICE OF APPEAL TO DISTRICT COURT

Onofre J. Sotelo and Naomi Sotelo, the bankrupts, and the appellants herein, appeal to the above-mentioned District Court from the order of the Bankruptcy Judge entered in this case 23 January 1976 as an order allowing the application of the trustee to pay a \$10,000 homestead exemption to the Internal Revenue Service.

The parties to the order appealed from and the names and addresses of their attorneys are as follows:

Representing the appellants herein:

Bruce L. Balch of
Katz, McAndrews, Durkee & Telleen
Attorneys at Law
402 First National Bank Building
P.O. Box 66
Rock Island, IL 61201

12a

Representing the Internal Revenue Service:

Donald B. Mackay, U.S. Attorney
Attn: Robert J. Kauffman,
Assistant U.S. Attorney
Federal Courthouse
Peoria, IL 61601

Representing the trustee in bankruptcy (pro se):

James E. Whitemire, Jr.
105 - 7th Street
Silvis, IL 61282
Dated: 23 January 1976

The above-mentioned appellants

By: /s/ Bruce L. Balch
BRUCE L. BALCH for
KATZ, MCANDREWS, DURKEE
& TELLEEN
Attorneys for Appellants
402 First National Bank
Building
P.O. Box 66
Rock Island, IL 61201
Telephone: 309/788-5661

13a

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS
NORTHERN DIVISION

RI-BK-73-233/234

IN THE MATTER OF
ONOFRE J. SOTELO and NAOMI SOTELO,
BANKRUPTS

NOTICE OF APPEAL

Notice is hereby given that Onofre J. Sotelo and Naomi Sotelo, the bankrupts herein, hereby appeal to the United States Court of Appeals for the Seventh Circuit from the "Decision and Order on Appeal" entered 23 February 1976.

ONOFRE J. SOTELO and
NAOMI SOTELO, Appellants

By: /s/ Bruce L. Balch
BRUCE L. BALCH of
KATZ, MCANDREWS, DURKEE
& TELLEEN
Attorneys for Appellants
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Building
P.O. Box 66
Rock Island, IL 61201
Telephone: 309/788-5661

14a

SUPREME COURT OF THE UNITED STATES

No. 76-1800

UNITED STATES, PETITIONER

v.

ONOFRE J. SOTELO and NAOMI SOTELO

ORDER ALLOWING CERTIORARI

Filed October 3, 1977

The petition herein for a writ of certiorari to the United States Court of Appeals for the Seventh Circuit is granted. The case is set for oral argument in tandem with No. 76-1835.